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CORPORATE FILE



ANNUAL REPORT / 1966

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Executive Vice President

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Chairman of the Board,
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Eagle-Picher Industries, Inc.

EDWARD D. SMITH
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The First National Bank of Atlanta



annual report 1966

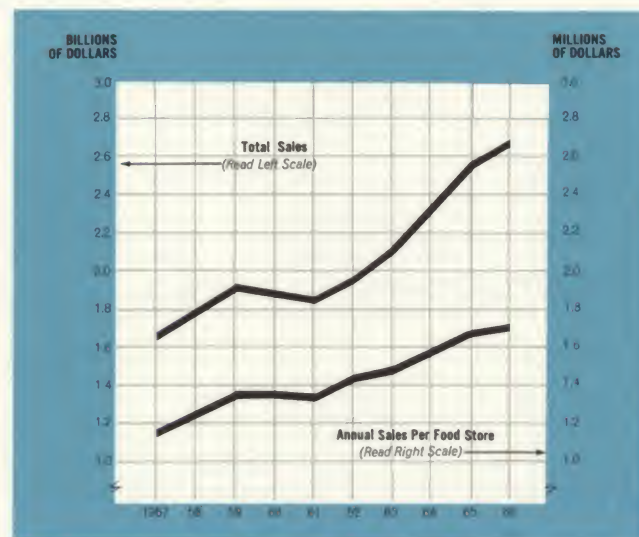
The Kroger Co.
1014 Vine Street
Cincinnati, Ohio 45201

Contents

Highlights.....	1
Letter to Shareowners.....	2
Balance Sheet.....	4
Income Statement.....	6
Sources and Uses of Funds.....	8
Ten Year Statistical Summary.....	9

Highlights

	1966	1965	Change
SALES	\$2,659,983,151	\$2,555,109,466	+4.1%
NET INCOME	\$ 28,516,694	\$ 31,302,137	—8.9%
NET INCOME PER SHARE	\$2.22	\$2.42	—8.3%
NET WORTH	\$ 253,293,632	\$ 244,958,043	+3.4%
NET WORTH PER COMMON SHARE	\$18.54	\$17.72	+4.6%
CAPITAL EXPENDITURES	\$ 66,626,426	\$ 44,489,193	+49.8%
DEPRECIATION AND AMORTIZATION	\$ 26,426,311	\$ 24,204,281	+9.2%



To Our Shareowners:

Sales again increased in 1966 but earnings declined.

Earnings

Net income for the 52-week year was \$28,516,694 or \$2.22 per share on the shares outstanding at year end, a decline of 8.3% from the \$2.42 per share earned in the 53 weeks of 1965.

Earnings are after Lifo charges of 12½¢ per share, as compared with 2½¢ per share last year. The Lifo inventory method reduces reported earnings in years of rising prices, but it reduces our federal income tax liability proportionately and enables us to retain additional cash for reinvestment in the business.

After-tax earnings benefited from the investment credit, equal to 24¢ per share, and from tax losses of certain subsidiaries carried forward from prior years. On the other hand, net income was reduced by a large number of early retirements. The Employees' Benefit Fund was increased by \$3,576,737. In 1967 and subsequent years your company will account for retirement expense in accordance with the provisions of Bulletin No. 8 issued by the American Institute of Certified Public Accountants in November, 1966. The new accounting rules require that a charge be made in each year for the estimated future retirement expense of all eligible employees on the payroll instead of providing only for employees who have actually retired, as Kroger has done heretofore. Had the new rules been in effect during 1966, we estimate that an additional provision in the area of \$1 million would have been required.

Dividends

Dividends of \$1.30 per common share were paid in

1966. This was the 65th consecutive year in which dividends were paid out of current earnings. The regular quarterly dividend of 32½¢, payable March 1, 1967, has been declared.

Sales

Sales of \$2,659,983,151 (52 weeks) exceeded 1965 (53 weeks) by 4.1%. Average annual sales per food store were \$1,706,128, an increase of \$39,509 over 1965.

Retail Food Divisions

Strongly competitive conditions prevailed throughout 1966. The prices paid by retailers for farm products and processed foods increased by substantially wider margins than retail food prices. In spite of improved equipment and methods, employee productivity did not keep pace with increases in wage rates. Kroger has been unable to reflect these higher costs of merchandise and wages in its retail price structure. Our retail prices must be competitive.

Several important changes were made during 1966 to make operations more efficient in future years. Our distribution centers in Milwaukee and Madison were closed. The Chicago warehouse now serves our Wisconsin stores in addition to those in the Chicago area. Similarly, the Pittsburgh distribution center was closed and Pittsburgh area stores are being served from Cleveland. While additional expenses were incurred to accomplish these consolidations, the combined facilities will enable us to distribute merchandise to our stores more economically than before.

New meat distribution plants were opened in several Kroger cities. Significant merchandising as well as operating gains will be realized from their use. There were 111 new food stores opened, 76 old ones closed,

and 114 existing stores remodeled. We had 1,493 food stores at the end of the year. The average size of the stores opened in 1966 was 14,671 square feet.

Drug Operations

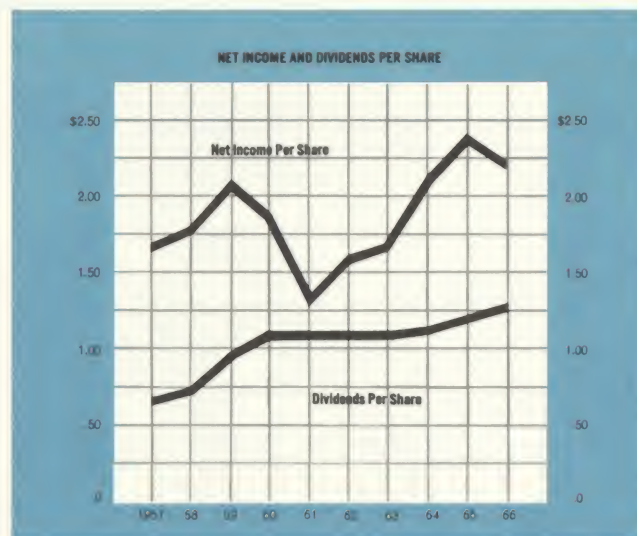
The drug division had another year of progress. Sales and earnings increased. There were 245 stores in operation at the end of 1966, after opening 67 stores and closing 2. SuperRx operations were extended to three additional states with the opening of 9 stores in California, 4 in North Carolina and 1 in Nevada. The new store program for 1967 will include Michigan where litigation to obtain pharmacy licenses has been successfully concluded.

Food Processing

Modernization of manufacturing plants continued in accordance with our long-range objective of having as efficient processing facilities as exist anywhere in the food industry. The Detroit dairy and ice cream plant is nearing completion and construction of a similar plant in St. Louis is under way. Equipment is now being installed in the new candy plant at our manufacturing complex in Springdale, Ohio, and construction has begun on a raw materials warehouse there. The line of Kroger manufactured products has been improved and enlarged to offer the consumer a wider choice of values.

Financial

Working capital at the year end was \$66,939,729, down from \$90,409,624 a year ago. The company incurred substantial interest expense on short-term loans during the year to meet seasonal inventory requirements and for capital expenditures. All loans were repaid by the



end of the year. An effective system of inventory control resulted in lower year-end inventories than in 1965 despite increased sales, a growing number of new products and higher unit costs.

Capital expenditures were \$66,626,426, of which \$10,061,405 was for store land and buildings, \$26,104,579 for store equipment and improvements, \$10,652,468 for distribution centers, \$7,581,803 for transportation equipment, \$8,871,527 for manufacturing facilities, and \$3,354,644 for other items. Depreciation and amortization totaled \$26,426,311.

Officers and Directors

W. George Pinnell, Dean of the Graduate School of Business of Indiana University, was elected a Director at the Annual Meeting in March. Gene D. Hoffman was elected Vice President in charge of manufacturing operations and Bennett A. Hudson was elected Vice President with responsibility for nine retail divisions.

Outlook for 1967

Your management is disappointed and dissatisfied with 1966 results. Current indications are that 1967 will be another year of intense competition. Nevertheless, we expect to make progress this year.

Sincerely,

Acote Davis

February 10, 1967

President



consolidated balance sheet

assets

	Dec. 31, 1966	Jan. 1, 1966
Cash.....	\$ 37,717,692	\$ 40,392,438
Marketable securities, at cost.....	—	23,463,692
Receivables.....	19,426,353	15,022,336
Inventories (Note 1).....	183,995,027	184,344,146
Store and general supplies.....	7,323,681	8,149,557
Prepaid and miscellaneous assets.....	7,717,730	6,553,321
TOTAL CURRENT ASSETS.....	256,180,483	277,925,490
Investments in unconsolidated companies (Note 2).....	2,772,135	3,550,296
Land, buildings and equipment, at cost or less.....	334,637,887	294,652,178
Less allowance for depreciation.....	(134,486,448)	(124,312,508)
Leaseholds and leasehold improvements, net.....	48,598,134	45,673,041
Excess cost of investment in subsidiaries over net assets acquired.....	13,325,279	13,327,759
TOTAL ASSETS.....	\$521,027,470	\$510,816,256

december 31, 1966 and january 1, 1966

liabilities

	Dec. 31, 1966	Jan. 1, 1966
Accounts payable.....	\$121,791,915	\$109,449,766
Accrued expenses.....	46,547,177	51,225,215
Accrued federal taxes.....	18,594,662	21,469,885
Long-term indebtedness (Note 3).....	2,307,000	5,371,000
TOTAL CURRENT LIABILITIES.....	189,240,754	187,515,866
Long-term indebtedness (Note 3).....	33,455,000	35,803,000
Deferred federal income taxes.....	30,125,000	30,830,000
Deferred investment credit.....	1,633,000	2,006,000
Employees' benefit fund.....	13,280,084	9,703,347
CAPITAL		
Preferred capital stock:		
First preferred, par \$100.....	24,000	24,000
Cumulative preferred, voting, par \$50 (Notes 4, 5 and 6)		
Authorized: 750,000 shares		
Outstanding: Series A; 1966—461,821 shares;		
1965—462,680 shares.....	23,091,050	23,134,000
Common capital stock, par \$1 (Notes 5 and 6)		
Authorized: 18,000,000 shares		
Issued: 1966—12,885,827 shares;		
1965—12,868,414 shares.....	62,061,519	61,706,506
Accumulated earnings (Note 3).....	184,068,980	172,750,812
	246,130,499	234,457,318
Less, common capital stock held in treasury, at cost:		
1966—470,594 shares; 1965—353,019 shares.....	15,951,917	12,657,275
	230,178,582	221,800,043
TOTAL CAPITAL.....	253,293,632	244,958,043
TOTAL LIABILITIES AND CAPITAL.....	\$521,027,470	\$510,816,256

Consolidated Statement of Income

Years Ended December 31, 1966 and January 1, 1966

	1966	1965
Sales	\$2,659,983,151	\$2,555,109,466
Cost of sales	2,135,174,190	2,051,494,555
Operating, general and administrative expenses	473,194,176	445,466,947
Total	<u>2,608,368,366</u>	<u>2,496,961,502</u>
Operating profit	51,614,785	58,147,964
Interest expense	3,213,091	2,035,827
Income before federal taxes on income	48,401,694	56,112,137
Federal taxes on income	19,885,000	24,810,000
Net income	<u>\$ 28,516,694</u>	<u>\$ 31,302,137</u>

Consolidated Statement of Accumulated Earnings

Years Ended December 31, 1966 and January 1, 1966

Accumulated earnings—Beginning of the year	\$ 172,750,812	\$ 157,840,360
Net income for the year	28,516,694	31,302,137
	<u>201,267,506</u>	<u>189,142,497</u>
Dividends:		
Preferred	994,195	1,003,977
Common	16,204,331	15,387,708
	<u>17,198,526</u>	<u>16,391,685</u>
Accumulated earnings—End of the year (Note 3)	<u>\$ 184,068,980</u>	<u>\$ 172,750,812</u>

notes to financial statements

1. Inventories are valued at the lower of cost, in part on a Lifo basis, or market.
2. The financial statements include the accounts of the company and all of its subsidiaries, except: Top Value Enterprises, Inc. (66.75% beneficially owned); and two other companies which are insignificant in the aggregate. The company's investment in Top Value is stated at cost of \$778,459, and its equity in the net assets at December 31, 1966 and earnings for 1966 were \$6,663,415 and \$813,426, respectively. No dividend was received. The investment in and advances to the other unconsolidated subsidiaries and the affiliates are stated at cost of \$1,993,676.

3. Long-term indebtedness:

3.1% notes maturing in 1971	\$ 9,800,000
4¾% notes, 70% maturing in 1978, 30% maturing in 1979	8,650,000
4.8% notes maturing in 1981	14,250,000
5½% notes maturing in 1977	1,600,000
Other	1,462,000
	<u>35,762,000</u>
Less, amounts due within one year	2,307,000
	<u>\$33,455,000</u>

Under certain of the loan agreements, payments of cash dividends are limited. At December 31, 1966, accumulated earnings unrestricted, under the agreement carrying the maximum limitation, amounted to \$83,216,458.

4. As of December 31, 1966, 475,066 shares of the authorized Cumulative Preferred Shares are designated Series A. These shares provide for annual dividends of \$2.15 per share; con-

version into Common Stock, until September 30, 1973, at one and one-half shares for each share of preferred; and redemption at \$55 per share to September 30, 1968, and \$50 per share thereafter, plus accumulated and unpaid dividends.

5. Options to officers and executives to purchase 415,235 shares of Kroger Common Stock were in force at January 1, 1966. Option transactions during 1966 may be summarized as follows: granted 134,000 shares; exercised 15,486 shares; expired or cancelled 23,384 shares. Options to purchase 510,365 shares were in force at December 31, 1966. Shares available for option at the beginning and close of the year were 170,100 and 43,100, respectively. Options for 205,205 shares were exercisable at December 31, 1966. Options to Market Basket employees to purchase 4,691 Kroger Cumulative Preferred Shares, Series A, were in force at January 1, 1966. Option transactions during the year 1966 may be summarized as follows: exercised 426 shares; expired or cancelled 374 shares. Options to purchase 3,891 shares were in force at December 31, 1966. There were no shares available for option at the beginning or close of the year. Options for 2,537 shares were exercisable at December 31, 1966.
6. At December 31, 1966, 698,569 shares of authorized Common Stock are reserved for conversion of Cumulative Preferred Shares, Series A.
7. The company operates principally in leased premises. Aggregate minimum annual rentals are approximately \$45,870,000 of which \$33,040,000 relates to leases outstanding at December 31, 1966, and expiring subsequent to 1971. Lease terms generally range from 10 to 25 years with options of renewal for additional periods. Options provide in some cases for renewals at reduced rentals and/or the right to purchase.

Report of Certified Public Accountants

To the Board of Directors
The Kroger Co.

We have examined the consolidated balance sheet of The Kroger Co. and subsidiary companies as of December 31, 1966, and the related consolidated statements of income and accumulated earnings for the fiscal year (fifty-two weeks) then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We previously examined and reported

upon the consolidated financial statements of the company and subsidiary companies for the year 1965.

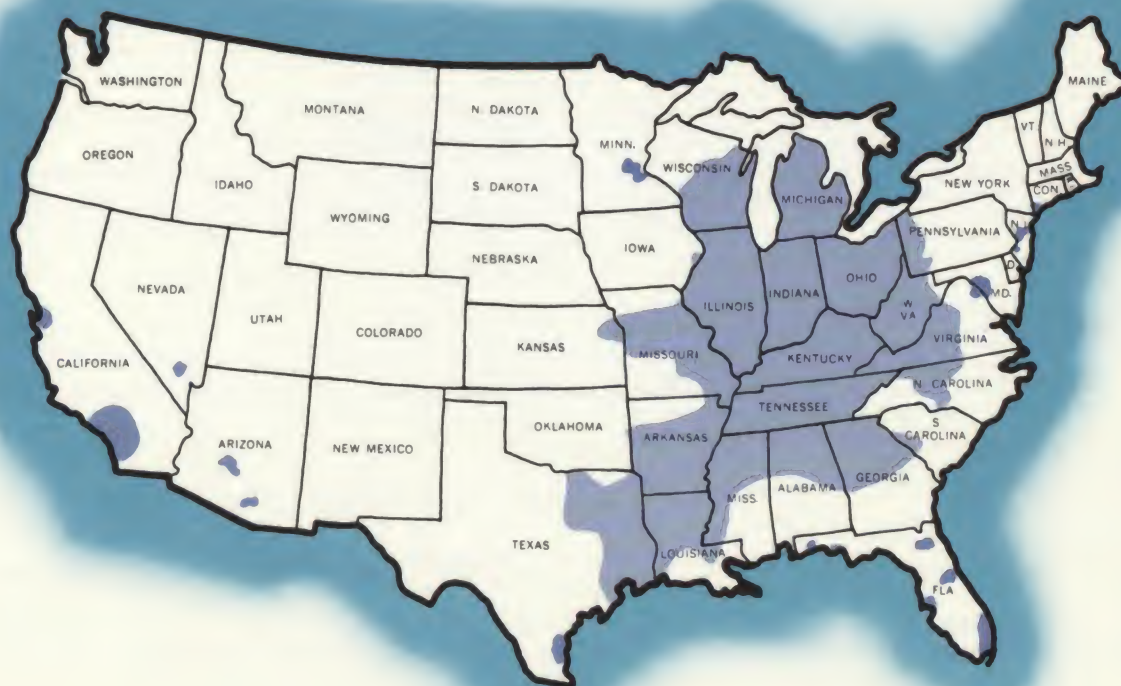
In our opinion, the accompanying financial statements present fairly the consolidated financial position of The Kroger Co. and subsidiary companies at December 31, 1966 and January 1, 1966 and the consolidated results of their operations for the fiscal years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Cincinnati, Ohio
February 10, 1967

Edward Lee Bess, Jr. & Montgomery

sources and uses of funds

	Year Ended	
	Dec. 31, 1966	Jan. 1, 1966
SOURCES OF FUNDS		
From current operations:		
Net income for the year.....	\$ 28,516,694	\$ 31,302,137
Charges to income not requiring funds:		
Depreciation and amortization.....	26,426,311	24,204,281
Provision for employees' benefit fund—net.....	3,576,737	2,544,334
Provision for deferred income taxes.....	(705,000)	1,050,000
Capital stock issued under stock option plans.....	309,737	1,695,397
Sale of capital assets subsequently leased back.....	4,587,496	—
Net book value of capital asset disposals.....	2,650,793	2,481,455
Total Sources.....	<u>\$ 65,362,768</u>	<u>\$ 63,277,604</u>
USES OF FUNDS		
Capital expenditures.....	\$ 66,626,426	\$ 44,489,193
Dividends paid.....	17,198,526	16,391,685
Purchases of treasury stock.....	3,289,308	6,880,421
Reduction in long-term indebtedness.....	2,348,000	5,431,292
Other changes—net.....	(629,597)	1,947,268
Total Uses.....	<u>\$ 88,832,663</u>	<u>\$ 75,139,859</u>
NET CHANGE IN WORKING CAPITAL.....	<u>\$ (23,469,895)</u>	<u>\$ (11,862,255)</u>
Working capital, beginning of the year.....	90,409,624	102,271,879
WORKING CAPITAL, END OF THE YEAR.....	<u>\$ 66,939,729</u>	<u>\$ 90,409,624</u>



COMMON STOCK

TRANSFER AGENTS

The First National Bank,
Cincinnati
Bankers Trust Company,
New York

REGISTRARS

The Central Trust Company,
Cincinnati
Chemical Bank New York
Trust Company, New York

CUMULATIVE PREFERRED STOCK—SERIES A

TRANSFER AGENT
Bank of America,
Los Angeles

REGISTRAR

Crocker-Citizens National Bank,
Los Angeles



10 year statistical summary

for the year

	SALES	NET INCOME BEFORE TAXES	NET INCOME	NET INCOME PER SHARE (1)	DIVIDENDS PER SHARE (2)	RETAINED EARNINGS
1966	\$2,659,983,151	\$48,401,694	\$28,516,694	\$2.22	\$1.30	\$11,318,168
1965	2,555,109,466	56,112,137	31,302,137	2.42	1.22½	14,910,452
1964	2,327,563,209	54,449,271	27,923,271	2.14	1.12½	12,695,198
1963	2,102,106,248	45,083,898	22,078,898	1.73	1.10	7,910,912
1962	1,947,570,909	44,219,055	20,424,055	1.62	1.10	6,578,540
1961	1,842,342,667	35,035,685	16,952,685	1.34	1.10	3,094,323
1960	1,870,289,637	48,218,029	23,478,029	1.87	1.10	9,732,605
1959	1,911,902,467	54,137,920	25,516,920	2.06	.95	13,751,230
1958	1,776,175,147	44,432,930	21,629,930	1.76	.72½	12,739,263
1957	1,674,123,593	41,505,207	20,635,207	1.70	.66⅔ (3)	12,866,895

at the year end

	CASH	INVENTORIES	WORKING CAPITAL	NET FIXED ASSETS	ACCUMULATED EARNINGS	NET WORTH
1966	\$37,717,692	\$183,995,027	\$ 66,939,729	\$248,749,573	\$184,068,980	\$253,293,632
1965	40,392,438	184,344,146	90,409,624	216,012,711	172,750,812	244,958,043
1964	54,202,675	169,500,867	102,271,879	198,357,132	157,840,360	235,238,796
1963	50,679,173	156,420,181	93,949,169	190,954,622	145,145,162	224,592,415
1962	55,925,833	131,832,323	82,085,737	174,684,454	137,234,250	194,303,798
1961	64,004,006	121,395,266	95,694,906	169,967,219	130,655,710	188,884,685
1960	47,354,159	118,783,384	77,681,795	164,214,971	127,561,387	185,077,175
1959	52,865,583	118,862,668	93,854,922	145,970,482	117,828,782	173,461,086
1958	52,566,148	116,628,932	86,679,309	130,504,808	104,077,552	158,573,593
1957	42,927,467	111,474,382	73,136,938	108,866,641	91,338,289	143,730,410

	NET WORTH PER COMMON SHARE (1)	NUMBER OF SHAREOWNERS	NUMBER OF EMPLOYEES	NUMBER OF FOOD STORES	ANNUAL SALES PER FOOD STORE	TOTAL FOOD STORE AREA (Sq. Ft.)
1966	\$18.54	45,411	41,462	1,493	\$1,706,128	24,095,663
1965	17.72	40,804	39,997	1,458	1,666,619	23,196,320
1964	16.81	41,602	39,785	1,431	1,582,359	22,295,587
1963	15.94	42,904	39,130	1,424	1,476,223	22,026,900
1962	15.39	39,936	37,440	1,364	1,433,091	19,841,911
1961	14.96	36,368	37,308	1,354	1,349,702	18,939,624
1960	14.75	35,663	39,691	1,372	1,357,249	18,264,615
1959	13.97	34,972	40,157	1,393	1,357,885	17,392,580
1958	12.87	28,514	40,500	1,428	1,257,914	16,805,232
1957	11.83	26,583	39,389	1,421	1,157,006	15,092,774

(1) Adjusted for 3 for 1 split in 1958 and 4% common stock dividend in 1957.

(2) Adjusted for 3 for 1 split in 1958.

(3) Plus 4% stock dividend.

